Court of Appeals of Kentucky.

W. R. THOMPSON, APPELLANT, *v.* MARY TENLEY, APPELLEE.

In Kentucky, negotiable paper, unless discounted at a bank, passes subject to all equities existing between the parties. Where it is given for the price of land, the vendor executing a deed, with full covenants of warranty of title, the land being at the time encumbered by a mortgage or vendor's lien, the purchaser will be entitled, in equity, to set off the amount of the mortgage against his notes, if before the notes become due the vendor has become insolvent. And the vendee, having said to one who had the notes for sale, that they "were all right," will not preclude him from making such defence.

The opinion of the court was delivered by

LINDSAY, J.—If the note sued on in this action still belonged to Pearson, the payee, it is manifest that Thompson would have the right to demand that the mortgage-lien owned by Mayo should be extinguished before judgment should go against him for the balance now in litigation, unless Pearson could show that it was part of the contract between himself and Thompson, that the latter, in addition to the two notes for $3000 each, was also to pay off and satisfy the mortgage-debt.

The acceptance of a deed with general warranty would not preclude Thompson, in a contest with Pearson, the latter being insolvent, from demanding a clear and unencumbered title before paying the purchase-money, and the right to make this demand would not depend upon Thompson's knowledge of the defect of title, nor of Pearson's insolvency at the time of the acceptance of the deed, but upon the existence of the defect and the insolvency at the time Pearson should seek a specific execution of the contract of purchase, *i. e.* the payment of the purchase-money.

The distinction between the case of a plaintiff seeking a specific performance in equity and a defendant resisting such performance, is well defined and universally recognised: Story's Eq. Jur., sect. 769; *Hatcher and Wife* v. *Andrews, &c.*, 5 Bush 561. There is no proof conducing to show that Thompson agreed to pay off the mortgage debt, the recital in the deed that $3000 were paid in cash, when in point of fact no such payment was made, is a circumstance from which the inference might be drawn that something more than $6000, the amount of the two notes, was to be paid for the property, but in the absence of direct evidence that such was the case, and in view of the positive and uncontradicted statements

of Thompson to the contrary, this inference cannot be allowed to charge him with the payment of the mortgage debt.

The testimony of Mayo establishes only that Thompson told him that his claim would be paid when the arrangement for the purchase was consummated, or that Thompson had loaned or expected to advance some money to Pearson, to enable him to release the mortgage lien. This evidence rather tends to rebut the presumption that Thompson was himself to satisfy the mortgage, and harmonizes with his statement that Pearson agreed to pay Mayo out of the first moneys realized by a sale of the notes. The evidence of Davis also conduces to show that Pearson had made this agreement. He states that in the conversation he had with Thompson when contracting for the property, the latter informed him that Pearson had promised to pay off Mayo's mortgage, but that he did not know whether he had done so or not. Thompson did not state to Davis that he would lose money on the property in selling it for $8500, but that if he had to pay off the mortgage, the paving claims, and the full amount of the note sued on in this action, that he would in that event lose money.

So far we have considered this case as though Pearson was the plaintiff. As to the matters considered Mrs. Tenley occupies no more favorable attitude than he would have occupied. The assignment to her did not impair Thompson's right to any defence, discount or offset he might have used against Pearson. It remains now to be determined whether Thompson is estopped to make the defence relied on, and whether he by promises to pay the note prevented Mrs. Tenley from discounting it, and thereby placing it upon the footing of a bill of exchange. The only statement made by Thompson before the purchase of the note by appellee, from which it could possibly be inferred that he had no defence, set off or counter claim on which he could or would rely to defeat its collection, was the conversation with Green, the clerk of Norton, Gault & Co., with whom Pearson had left the note to be sold. When asked by Green if the note was all right, Thompson replied, "Of course it is all right, if I had not thought it was all right I would not have given my notes." Green did not tell Thompson the name of any person who was negotiating for the note, nor did Green ask for, or Thompson give him authority to repeat this conversation to persons to whom he might offer to sell it. Green was the agent of Pearson and not of appellee. The

statements or assurances made by Thompson to Green are no more binding upon him than they would have been if made to Pearson himself. Besides this, there is no evidence that the note was purchased upon the faith of those statements. Green states that Tenley, the agent of appellee, said to him, that relying upon Thompson's representations he would buy the notes, but Tenley's deposition is not taken, and we have no means of knowing whether he relied on these representations or upon his own judgment. In the case of *Smith* v. *Stone*, 17 B. Mon. 168, the assignee purchased the note in consequence of representations made to his agent. In the case of *McBryer* v. *Collins*, 18 B. Mon. 833, the payer of the note represented to the assignee himself that it was good. We have found no case in which the payer has been estopped to make defence, because of statements made to the payee or to the payee's agent, and conceive that the doctrine will never be carried to that extent, unless it can be shown that he constituted them his agents, and expressly authorized them to repeat his statements to persons to whom they might propose to sell the note. No such express agency can be inferred from the street conversation between Thompson and Green. It is therefore immaterial so far as Thompson's legal rights are concerned, whether Tenley did or not rely on the statements made to Green.

There is absolutely no proof conducing to show that Thompson promised to pay the note after the assignment, except what he himself says as to his conversation with the cashier of the Farmers and Drovers' Bank, where the note was left for collection. A day or two before it became due, he "asked if the bank had discounted it, and if so, whether it could be renewed. The reply was "that the bank had not discounted it, but that Mr. Abbott had left it there, and to see him." He went again on the day the note was due, "and was told that Mr. Abbott had said the note could not be renewed by my giving security." From this it is clear that Thompson did not agree to pay the note, and did nothing calculated to prevent appellees from discounting it. Nor does it matter that Thompson did not see Abbott about the renewal, as he, Abbott, had left word at the bank that he would not be permitted to renew it. We are of opinion that Thompson has made out a good defence to so much of the note as is now being litigated, and that he has been guilty of no act that estops him from relying upon such defence; there are other matters can-

vassed by counsel, but as they are not material to the issues involved, they will not be considered by the court.

Opinion by LINDSAY, J., on petition for rehearing.

In the cases of *Ridgway* v. *Collins*, 3 A. K. Marshall, and *Robbins* v. *Hally*, 1 Monroe, there was no connection between the demands sought to be set off against each other. In each case the court notices this fact, and gives it as one of the reasons, why relief will not be granted.

In the case of *Daviess* v. *Newton*, 5 J. J. Marshall 90, the court recognises the right, where the demands are connected, to have them set off, even though the assignor of the note had removed from the state or became insolvent after notice of assignment.

In this case the demands are not only connected and growing out of the same transaction, but Thompson defends upon a ground always recognised in equity. He is resisting the specific execution of a contract for the sale of realty, because of defect of title and the insolvency of his vendor.

When Thompson accepted Pearson's deed, he did not waive his right to insist that encumbrances on the title should be removed before paying the purchase-money, in case his warrantor became insolvent before the same became due and payable. Pearson could not deprive him of this right by assigning the note.

Appellant sued on the note three days after it was due. Thompson answered a month afterwards, setting up Pearson's insolvency. His answer was treated as good and the cause prepared and tried upon its merits. This court is of opinion that a good defence was made out, and is not disposed to deprive Thompson of the benefit of the defence because he did not specifically allege that Pearson was insolvent on the day the note fell due, it being evident that the Chancellor and the appellee regarded and treated the pleadings as sufficiently specific and direct.

It is not shown that Thompson executed the notes for the purpose of enabling Pearson to raise money by selling them.

The petition for a rehearing must be overruled.

The foregoing case is somewhat imperfectly stated, in regard to the facts, but still we think sufficiently so to render the decision intelligible. The purchaser of the land attempts, in equity, to set off the amount of the encumbrance upon the land, at the time of the purchase, against the price of the land, for which he had given his promissory notes. As negotiable paper in that state

possesses no peculiar immunity against equitable defences, as between the original parties, this case stands, primarily, the same as if the note were sued in the name of the original payee.

In such a case it is unquestionably equitable, for the mortgage to be deducted from the price, and only the remainder enforced against the purchaser. This will in fact, reach the exact justice of the case and save circuity of action by means of the vendor's covenants of warranty. But still no such defence is strictly allowable at law. There being no fraud in the case there is no ground to claim a rescinding of the contract: *Thornton* v. *Wynn*, 12 Wheat. 183; *West* v. *Cutting*, 19 Vt. 537. The breach of the covenants of warranty of title, can at most, only show a partial failure of consideration of the notes, and one which the parties provided for in their contract by the covenants in the deed. Unless, therefore, the purchaser had paid off the encumbrance before suit brought upon the notes, he could not enforce a set-off by means of the breach of the covenants. The only remedy would be in a court of equity. And here the remedy is ample, provided the counter claims are in fact mutually in equity, although not so in form, or at law. Equity will, in such cases, always interfere in case of insolvency: *Blake* v. *Langdon*, 19 Vt. 485, where the cases are carefully cited and compared. The result of which is: 1. That courts of equity decree set-off, anterior to and independent of the statutes of set-off: *Ex parte Stephens*, 11 Vesey 24; *Ex parte Blagden*, 19 Id. 465; *Hawkins* v. *Freeman*, 2 Eq. Cas. Ab. 10, pl. 10. 2. That after the statute of set-off, 2 Geo. 2 and 5 Geo. 2, the courts of equity conformed their practice to the statute, except in cases of special equity: *Ex parte Quintin*, 3 Ves. 248. Cases of insolvency, and where otherwise one party will pay more than he really owes, and be left remediless, have always been regarded as justifying the interference of courts of equity to decree set-off. And other equitable grounds of interference are numerous: *Dale* v. *Cook*, 4 Johns. Ch. 13; 2 Story Eq. Jur., § 1432 *et seq.* Equity too might divide the debt of the appellant, and enable him to first pay the mortgage, then pay the remainder to the appellee: *Ex parte Quintin*, *supra*. How far the debtor's declaration will estop him from making the defence, is mainly matter of construction by the court, and is not liable to review. But it is obvious here that the appellant's language receives a very mild construction. We might about as well, as it seems to us, come to the opposite conclusion: See *Strong* v. *Ellsworth*, 26 Vt. 366.

I. F. R.

Circuit Court of the United States, Eastern District of Virginia.

AUGUSTUS HANCOCK ET UX. *v.* NEW YORK LIFE INSURANCE COMPANY.

The intervention of the late war was a sufficient excuse to the holder of a policy of life insurance, for not paying his premiums as they accrued during the war, the insurer being resident and domiciled upon one side of the military lines, and the insured upon the other.

A contract may be broken before the time for its performance arrives, by a party to it repudiating its obligation and declaring that he will not perform what he has bound himself to do.